Report to the Audit and Governance Committee

Report reference: AGC-002-2014/15
Date of meeting: 29 June 2015

Epping Forest District Council

Portfolio:	**Governance and Development Management**
Subject:	**Review of the Effectiveness of the System of Internal Audit**
Responsible Officer:	**Brian Bassington** (01992 564446).
Democratic Services:	**Gary Woodhall** (01992 564470).

Recommendations/Decisions Required:

(1)   The Committee is requested to note the following report for 2014/15 and the assurance level given:

(a)   The 2014/15 Audit Plan status report as at 31 March 2015 (Appendix 2);

(b)   To note the review of the effectiveness of the system of internal audit, undertaken by the Corporate Governance Group for 2014/15, in the context of the Council's Governance Statement; and

(c)   To scrutinise the review and consider the effectiveness of the system of internal audit in 2014/15.

Executive Summary:

This report is presented in support of the Internal Audit opinion on the adequacy of Epping Forest District Council's (EFDC) internal control environment, provides a summary of the work undertaken by the Internal Audit Unit between April 2014 and March 2015 and details the overall performance against the Audit Plan for 2014/15.

The Accounts and Audit Regulations include a requirement for the Authority to carry out an annual review of the effectiveness of its system of internal audit as part of the wider review of the effectiveness of the system of governance.

This report summarises the review undertaken for 2014/15 by the Corporate Governance Group, to assist the Committee in assessing the effectiveness of the system of internal audit on behalf of the Authority.

Reasons for Proposed Decision:

Monitoring report as required by the Audit and Governance Committee Terms of Reference.

To provide the Committee with the opportunity to scrutinise the review of effectiveness.

Other Options for Action:

No other options.

Report:

Introduction

1.   The Internal Audit Annual Report for 2014/15 is based on the Public Sector Internal Audit Standards (PSIAS) which came into force as from 1 April 2013. The work referred to in this report was carried out as part of the agreed Audit Plan for the period from 1 April 2014 to 31 March 2015.

2.   The purpose of the report is to support the Internal Audit opinion on the adequacy of Epping Forest District Council's (EFDC) internal control environment as a contribution to the proper, economic, efficient, and effective use of resources. This report provides part of the evidence that underpins the Corporate Governance Statement published in the Council's Statutory Statement of Accounts, in line with the requirements of the Accounts and Audit Regulations 2011.

Opinion

3.   The work of Internal Audit continues to improve awareness of governance requirements and to promote improvement in systems. Although overall full assurance cannot be given as risks cannot be totally minimised, the opinion given in this report provides a reasonable level of assurance that there are no significant weaknesses in the Council's control environment, as the audits carried out during 2014/15 concluded that systems were generally operating satisfactorily and appropriate follow up action has been taken where required to reduce risk of error or fraud.

4.   No material errors were identified from Internal Audit work carried out on the Council's major financial systems during 2014/15. Reviews of the Council's overall systems of internal control identified some weaknesses in internal controls which were referred to in reports to the Audit and Governance Committee, and in the Council's Governance Statement.

External Audit

5.   The Authority's External Auditor has a statutory responsibility to express an independent opinion on EFDC's accounts, performance management and the financial aspects of corporate governance. The External Auditors (BDO) were appointed by the Audit Commission, who have to be confident in the processes and procedures at EFDC to produce the accounts by the statutory deadline each year, as well as being able to place reliance on the work of Internal Audit. Internal and External Audit work closely together to avoid duplication of audit effort and to ensure that the Council receives comprehensive audit coverage.

The Role of Internal Audit

6.   Internal Audit is provided in the context of the Council's statutory responsibility to make arrangements for the proper administration of its financial affairs. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

7.   The main elements of the work are to:

        (a))   audit and report on the core financial controls throughout the Authority;

        (b))   provide advice during the development of new systems;

        (c))   provide advice on financial, contractual and IT controls, including Financial

Regulations and Contract Standing Orders;

(d))   review computer and network security;

(e))   investigate suspected fraud, corruption, bribery and other irregularities;

(f))   monitor the Anti-fraud strategy and participate in the National Fraud Initiative;

(g))   keep Management Board and the Corporate Governance Group informed of key issues;

(h))   liaise with the Audit Commission and their appointed External Auditors; and

(i))   report to the Audit and Governance Committee on key issues arising from audits and on the performance of the Audit team.

Performance against the Audit Plan

8.   Whilst the majority of planned audits, including all of the key audits of financial systems, were completed by 31 March 2015 nine audits have been carried forward into the 2015/16 plan due to changing circumstances within the Council such as the new waste management contract and a comprehensive review of debt management within the Council.

9.   During the year, 35 reports were issued to Management with the following assurance levels:

Assurance Level	2014/15	2013/14	2012/13
Full Assurance	4	4	1
Substantial Assurance	26	30	29
Limited Assurance	5	2	2
No Assurance	0	0	0

10.   The recommendations made within the audit reports are given a priority rating of 1 to 3, with priority 1 being the highest. The priority 1 recommendations are monitored by the Corporate Governance Group to ensure that action is taken and these actions are reported quarterly to the Audit and Governance Committee. The recommendations are included in detail as appendices to the four quarterly reports to the Audit and Governance Committee.

Priority Level	Number Issued 2014/15	Number Issued 2013/14	Number Issued 2012/13
Priority 1 - High	18	12	6
Priority 2 - Medium	44	41	31
Priority 3 - Low	24	12	12

Additional Support Provided

11.   To assist non-financially trained managers' understanding of finance and governance issues, advice is regularly given by the Audit team and a training course is provided by an external supplier supported by the Director of Resources and the Chief Internal Auditor.

12.   The level of assurance on the Council's systems of internal control that can be given by

the Chief Internal Auditor takes into account:

- All audit work completed during 2014/15;
- Follow up actions from previous years audits;
- Management's response to findings and recommendations;
- The resources available to deliver the audit plan;
- The certification of Service Directors in their assurance statements;
- Internal Audit performance in 2014/15;
- The reliance placed on the work of Internal Audit by the External Auditor; and
- Relevant information in Audit Commission and National Fraud Authority reports, such as Protecting the Public Purse and Fighting Fraud Locally.

13.   Taking all of the available information into account, in particular the audit work completed, it is considered by the Chief Internal Auditor that the Council has in place a satisfactory framework of internal control, which provides reasonable assurance regarding the efficient and effective achievement of its objectives in 2014/15.

Performance Management

14.   The Internal Audit Team has local performance indicator targets to meet in 2014/15, as set out below:

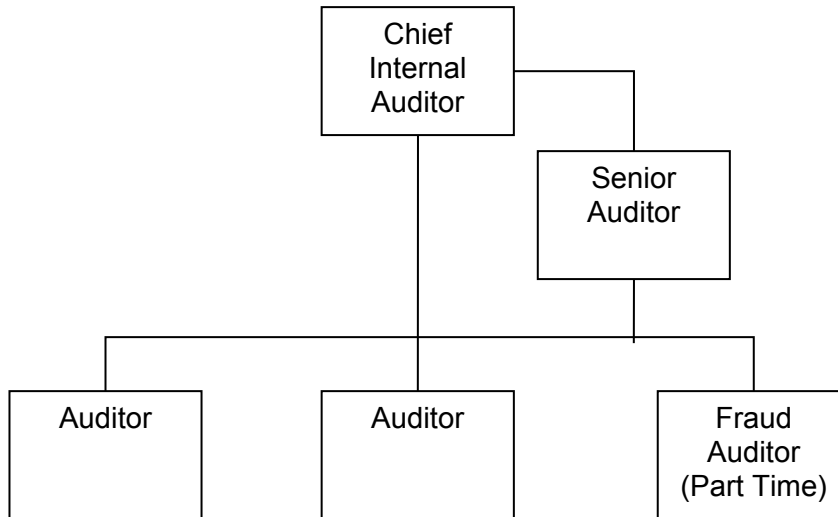|	Actual 2011/12	Actual 2012/13	Actual 2013/14	Target 2014/15	Actual 2014/15
% Planned audits completed	82%	85%	88%	90%	94%
% chargeable "fee" staff time	71%	69%	74%	72%	73%
Average cost per audit day	£213	£243	£225	£245	£218
% User satisfaction	89%	See note below	See note below	85%	98%

15.   The indicators are calculated as follows:

(a)   % Planned audits completed - a cumulative calculation is made based on the approved plan as amended for additional work (e.g. investigations) during the year.

(b)   % Chargeable fee time - a calculation is made based on reports produced from Internal Audit's time recording system.

(c)   Average cost per audit day - the calculation is based on the costs in the cost centre monitoring report divided by the number of fee earning days extracted from the time recording system.

(d)   User satisfaction has been based on a customer survey form which was replaced by an electronic form for use from April 2013. The rate of return did not improve with the new simplified form so Management were reminded of the importance of performance indicators and the need to complete and return the survey forms in a timely manner.

16.   These indicators are monitored by the Corporate Governance Group and the Audit and Governance Committee.

The Audit Team

17.   The Team currently has an establishment of 4.4 full time equivalent (fte) Internal Auditors.

18.   The establishment throughout 2014/15 is set out below:

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                    ┌──────────────┐
                    │    Chief     │
                    │   Internal   │
                    │    Auditor   │
                    └──────┬───────┘
                           │    ┌──────────────┐
                           │    │    Senior    │
                           │    │    Auditor   │
                           │    └──────┬───────┘
        ┌──────────────────┼──────────┴──────────┐
┌───────┴──────┐   ┌───────┴──────┐      ┌────────┴─────┐
│   Auditor    │   │   Auditor    │      │    Fraud     │
│              │   │              │      │   Auditor    │
│              │   │              │      │  (Part Time) │
└──────────────┘   └──────────────┘      └──────────────┘
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Review of the Effectiveness of Internal Audit

19.   Regulation 6 of the Accounts and Audit Regulations 2011 requires the Council to maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with proper internal audit practices. In EFDC the system of internal audit consists of the work of the Internal Audit Team, although supervisory processes in all Directorates provide a control and risk management function that could be defined as contributing to the system of audit. For this purpose, however, the work of the Internal Audit Team is seen as the focus of the review of effectiveness.

20.   The Council is required to carry out an annual review of the effectiveness of its system of internal audit, as part of a wider review of the effectiveness of the system of governance. It is the responsibility of the Authority to undertake the review, and not the External Auditor. The Audit and Governance Committee is the most appropriate body to oversee the review of the system of Internal Audit, as it is independent of the management of the Authority.

21.   The review should demonstrate that the Internal Audit service is:

        (a)   meeting its aims and objectives;

        (b)   compliant with the Public Sector Internal Audit Standards (PSIAS);

        (c)   effective, efficient and continuously improving; and

        (d)   adding value and assisting the Authority in meeting its objectives.

22.   The objective of these measures is to ensure that the performance and effectiveness of the Internal Audit service improves over time, in terms of both the achievement of targets

and the quality of service provided to the user.

23.   Along with compliance with the Standards, the review is to agree the effectiveness of the service. The outcome of the review is independent confirmation that the opinion in the annual report of the Chief Internal Auditor may be relied upon as a key source of evidence in the Governance Statement.

24.   The Council's External Auditors, BDO LLP conduct a thorough review of the quality of Internal Audit's work on financial systems for 2013/14, in assessing the extent of reliance that can be placed on the work, in the context of their audit of the Council's Statutory Accounts.

25.   The Annual Audit Letter 2013/14, issued by BDO in October 2014 stated that:

- an unqualified true and fair opinion on the financial statements was issued on 30 September 2014;

- the Council had implemented proper arrangements to secure economy, efficiency and effectiveness in its use of resources;

- the Annual Governance Statement was not inconsistent or misleading with other information we were aware of from our audit of the financial statements and complied with Delivering Good Governance in Local Government (CIPFA / SOLACE).

26.   The Council's Corporate Governance Group has undertaken the review of the Council's Internal Audit Service in 2014/15 utilising the following main sources of evidence:
- The annual report and opinion of the Chief Internal Auditor;
- A review of the Internal Audit Service against Public Sector Internal Audit Standards;
- A review of Internal Audit monitoring reports for 2014/15;
- Any comments from the Chief Executive following consideration of individual audit report summaries;
- The role of the Corporate Governance Group monitoring the work of Internal Audit and any significant internal control issues raised in their reports;
- Consideration of significant corporate control issues highlighted in audit reports, discussed within the Management Board;
- Performance by Internal Audit against local performance indicators;
- The Internal Audit section of the Governance Directorate Business Plan and work plans for 2014/15; and
- Assessment by the Audit Commission appointed auditors.

Summary of Findings

27.   The Internal Audit Section can demonstrate that it has a good understanding of the functions of the Council and has achieved the Council's objective to identify improvements to its control systems. The performance of the Unit has remained close to its key targets and while the actual audits achieved (94%) exceeded the target (90%) for completion of the audit plan. The Council's External Auditors found no inconsistencies in the work of Internal Audit when conducting their formal review of the Team's work as part of their review of the 2013/14 accounts.

28.   The Internal Audit Section now fully meets the Public Sector Internal Audit Standards introduced in April 2013 in that the quality assurance and improvement programme and Internal Audit Charter required by the standards were adopted by the Audit and Governance Committee at the meeting held on 25 September 2014. The standards require an internal annual review of compliance with the standards and external assessments must be conducted at least once every five years. The external assessments are part of discussions within the Essex Audit Group as to

the way forward in providing assistance between Essex authorities.

29. The work of the Audit and Governance Committee, with independent membership, makes an important contribution to the independent review of internal and external audit processes, as part of the Council's arrangements for securing further improvements in its systems of governance, including internal control. The Annual Report of the Audit and Governance Committee for 2014/15 demonstrated the range of issues addressed during the year.

30. In the opinion of the officers attending the Audit and Governance Committee, the continued support given by Members, in particular by insisting on timely and positive responses to audit recommendations, is invaluable in reinforcing the message of sound governance.

31. Having considered these issues, the Corporate Governance Group is satisfied that the Authority's system of Internal Audit was effective during 2014/15.

Resource Implications:

Within the report.

Legal and Governance Implications:

Within the report.

Safer, Cleaner and Greener Implications:

No specific implications.

Consultation Undertaken:

Corporate Governance Group.

Background Papers:

Audit files and working papers.

Risk Management:

Internal Audit has a primary objective to provide an independent and objective opinion on the adequacy of the Council's control environment, including its governance and risk management arrangements. The audit reports referred to in this report assist managers to determine the adequacy and effectiveness of the arrangements in place in their services.

Due Regard Record

This page shows which groups of people are affected by the subject of this report. It sets out how they are affected and how any unlawful discrimination they experience can be eliminated. It also includes information about how access to the service(s) subject to this report can be improved for the different groups of people; and how they can be assisted to understand each other better as a result of the subject of this report. S149 Equality Act 2010 requires that due regard must be paid to this information when considering the subject of this report.

Date / Name	Summary of equality analysis
1/5/15 Chief Internal Auditor	The report is a summary of the work carried out by Internal Audit and has no equality implications.

Audit Assurance Levels and Priority Ratings   Appendix 1

Priority Ratings
Each audit finding will generate an audit recommendation. These recommendations will be prioritised in accordance with the following criteria:

Priority 1 – Observations refer to issues that are fundamental to the system of internal control. We believe that these issues have caused or will cause a system objective not to be met and therefore require management action as a matter of urgency to avoid risk of major error, loss, fraud or damage to reputation. Failure to apply a Financial Regulation or Contract standing Order will normally be in this category.

Priority 2 – Observations refer mainly to issues that have an important effect on the system of internal control but do not require immediate management action. System objectives are unlikely to be breached as a consequence of these issues, although Internal audit suggested improvement to system design and / or more effective operation of controls would minimise the risk of system failure in this area.

Priority 3 – Observations refer to issues that would if corrected, improve internal control in general and ensure good practice, but are not vital to the overall system of internal control.

Assurance levels:
The level of assurance to be applied will be based on the auditor's assessment of the extent to which system objectives are met, with the agreement of the Chief Internal Auditor. As a guide, the following triggers will be used, taking into account the level of risk of error, loss, fraud or damage to reputation.

Overall assignment rating	Level of assurance and definition Trigger (number of individual audit recommendations)
1 Full Assurance –	There is a sound system of control designed to achieve system objectives, and the controls are being consistently applied. **Priority 3's or no audit recommendations**.
2 Substantial Assurance –	There is a sound system of control designed to achieve system objectives, and the controls are generally being consistently applied. However, there are some minor weaknesses in control, and/or evidence of non-compliance, which are placing some system objectives at risk. **Priority 2's and 1 Priority 1 (if assessed as a low risk).**
3 Limited Assurance –	There is a system of control in place designed to achieve system objectives. However, there are significant weaknesses in the application of control in a number of areas, and / or evidence of significant non-compliance, which are placing some system objectives at risk. **Between 1 and four 1's and (usually) several Priority 2's.**

4 No Assurance –   The system of control is weak, and / or there is evidence of significant non-compliance, which exposes the system to the risk of significant error or unauthorised activity.
Five or more Priority 1's.

Approved by the Audit and Governance Committee 15th November 2010

AUDIT PLAN 2014/15

Key	Risk Identifier			
AC	Audit Commission			
FFS	Fundamental Finance System			
R no.	Risk No. in Corporate Register			
R	Reputation of Council			

Audit area	Audit type	Days allocated	Completed	Risk Identifier
Resources				
Accountancy				
Bank Reconciliation	system/follow up	15	Completed	FFS
Sundry Debtors	system/follow up	15	Completed	FFS
Creditors	system/follow up	15	Completed	FFS
Treasury Management	system/follow up	10	Completed	FFS/R4
Budgetary Control (capital and revenue)	system/follow up	10	Completed	FFS
Insurance (Fraud)	Fraud	5	Completed	FFS
Main Accounting and Financial Ledger	system/follow up	15	Completed	FFS
Risk Management	system/follow up	5	Completed	FFS
Provision for 'top up' testing	systems	30	Completed	FFS
Benefits				
Housing Benefits	system/follow up	15	Completed	FFS
Council Tax Reduction	system/follow up	15	Completed	FFS
Revenues				
Council Tax	system/follow up	20	Completed	FFS/R4/AC
Business Rates	system/follow up	20	Completed	FFS/R4
Cash receipting and Income control	system/follow up	15	Completed	FFS
Human Resources				
Payroll	System/follow up	20	Completed	FFS
Recruitment and Selection	verification	10	Carried Fwd	R
Management of Sickness absence	verification	10	Completed	R
Overtime and Committee Allowances	verification	10	Completed	R
Travelling & Subsistence Claims	verification	10	Completed	R
Car Mileage claims	verification	10	Completed	R
Reprographics	System	10	Completed	
ICT and Facilities Management				
ICT Procurement	ICT	10	Carried Fwd	AC/R6
Access controls	ICT	10	Completed	R6
Facilities Management Contracts	system	10	Completed	AC
TOTAL		**315**		
Governance				
Governance and Performance Mgmt.				
Key and Local Performance Indicators	verification	15	Completed	R

Business Plans	verification	10	Completed	R
Equality Analysis	verification	10	Carried Fwd	R
Gifts and Hospitality (Members & Officers)	system/follow up	10	Completed	R
Legal				
Debt recovery	Follow up	10	Carried Fwd	R4
Development Management				
Planning Fees	System	20	Completed	R4
TOTAL		**75**		
Neighbourhoods				
Neighbourhood Services				
North Weald airfield	establishment	15	Completed	R4
Technical Services				
Waste Management and Recycling	system	20	Carried Fwd	R
Car Parking Contract	system	10	Completed	R4
Fleet Operations income	system	5	Completed	R4
Forward Planning & Economic Devel.				
Commercial Property portfolio	Follow up	10	Completed	R2
TOTAL		**60**		
Communities				
Housing Property				
Housing Repairs Service	system	20	Completed	R
Council Housebuilding Programme	system	15	Carried Fwd	AC
Housing Contracts	follow up	5	Carried Fwd	AC
Housing Operations				
Housing Rent Collection and Arrears	system/follow up	20	Completed	FFS/R4
Norway House/Rental Assistance Loans	Estab/system	10	Completed	R4
Private Sector Housing & Comm. Support				
Right to Buy	system	10	Completed	AC
Private Sector Housing - Grants	system	15	Completed	AC
TOTAL		**95**		
FRAUD PREVENTION & DETECTION				
Contracts	fraud	15	Carried Fwd	AC
Procurement	fraud	15	Completed	AC
Council Tax Discounts	fraud	15	Carried Fwd	AC
National Fraud Initiative (NFI)	fraud	20	Completed	AC
Data matching and analysis (IDEA software)	fraud	25	Completed	AC
TOTAL		**90**		
CORPORATE				

Corporate Procurement	system/follow up	15	Completed	AC
Corporate Asset Register	system	5	Completed	FFS
Priority 1 Audit recommendations	follow up	10	Completed	R
Governance Statement	management review	5	Completed	R
TOTAL		**35**		
TOTAL DAYS ALLOCATED		**670**		
Contingency/Minor investigations		**40**	Completed	
Corporate/Service Advice		**65**	Completed	
TOTAL		**775**		